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NABE Policy Survey

BUSINESS ECONOMISTS EXPECT 1990 BUDGET TARGET WILL NOT BE MET; ARE SATISFIED WITH FEDERAL RESERVE POLICY ACTIONS; FEEL THE THRIFT RESCUE BILL SHOULD BE ON BUDGET

June 1989

This report presents the results of a survey on economic policy issues made by nearly 300 business economists in early-June 1989. The **Economic Policy Survey** *is one of three surveys taken during each calendar quarter by NABE; the other surveys are the* **Industry Survey** *and the* **NABE Outlook**.

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Highlights from the June Survey

* The NABE panel overwhelmingly expected that the actual federal budget deficit for 1990 will be above the Gramm-Rudman-Hollings target of $99 billion. The average estimate of the 1990 budget deficit by the panel members was $129 billion. The panel had a sizable majority in favor of freezing military expenditures, while a significant fraction felt that military spending should be reduced. Most of the panel also felt that tax increases were an appropriate step in reducing the budget deficit, with most respondents advocating larger increases than the $5.3 billion in the House and Senate budget resolutions.

* The NABE panel continued to believe that the Federal Reserve is carrying out the correct monetary policy, although a larger fraction than in previous surveys felt that the Fed was being too restrictive. Given the expectations of slower economic growth for 1989, most of the panel expected the Fed to either keep monetary policy relatively unchanged or to ease policy modestly.

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* Nearly two-thirds of the panel felt that the cost of the FSLIC rescue bill should be on budget, with the resulting debt being issued by the Treasury Department rather than an off-budget agency. In addition, a majority of the NABE panel felt that the cost of the rescue plan should count against the Gramm-Rudman-Hollings deficit targets. A significant majority of the panel believed that the thrift industry should be restructured in major ways, including: having thrifts pay for a portion of the costs of the plan through higher deposit insurance rates, imposing risk-based capital guidelines on thrifts, and separating the regulatory and credit functions of the Federal Home Loan Bank Board.

1990 Budget Deficit and Budget Policy

The NABE policy panel had grave doubts that the 1990 federal budget deficit will fall within the Gramm-Rudman-Hollings limits, with only 8 percent of the respondents expecting the deficit to be less than or equal to the $99 billion target. The average forecast by the panel for the deficit was $129 billion, close to the median estimate of $127 billion.

Looking at the House and Senate budget resolutions, the NABE panel felt strongly that military spending should not be increased, as nearly 65 percent of the respondents agreed with the freeze on military expenditures contained in the budget resolutions. Another 29 percent felt that military spending should be cut. Not all spending categories should be subject to freezes or reductions according to the panel, however, as about two-thirds of the business economists felt that the increases in education, science, and space programs in the budget resolutions were justified or that they should be increased by even more than the resolutions called for.

In comparing the budget resolutions, more of the panel favored the Senate proposal -- which called for more spending on law enforcement and transportation programs -- than the House proposal -- which called for more spending on veteran's programs, aid to the poor, and spending on retirees. Even the Senate version gained the support of only 44 percent of the panel, though, with nearly one-third favoring either freezes or cuts in all of these areas. Both budget resolutions contained asset sales as a mechanism for reducing the deficit, but only 18 percent of the NABE panel felt that this was an unambiguously appropriate way to cut the deficit. Another 37 percent felt that asset sales were sometimes an appropriate way to cut the deficit, while a plurality of respondents, 45 percent, felt that asset sales were never an appropriate means of cutting the budget deficit.

When asked, "Should taxes be increased as a way to cut the budget deficit," 64 percent of the panel responded affirmatively, and of those an overwhelming 87 percent felt that taxes should be raised by more than the $5.3 billion called for in the budget resolutions.

Interestingly, in light of President Bush's recent major speech on the environment, about 70 percent of the respondents agreed with the auctioning of pollution rights concerning chlorofluorocarbons -- with 53 percent arguing for expansion of this program so that the "economically correct" level of pollutants would be produced. Finally, 80 percent of the NABE panel agreed with the House version's change in the tax laws so that the FDIC would include foreign deposits in U.S. banks when calculating deposit insurance premiums.

Monetary Policy

The respondents in the NABE policy survey strongly continue to favor the thrust of Federal Reserve monetary policy. Seventy-four percent said that the policy was "about right". A growing portion, however, felt that the Fed was being too restrictive in its conduct of monetary policy. Over the past year, covering four policy surveys, the percentage that felt that the Fed was being too tight has increased steadily from 6 percent at the end of the third quarter of 1988 to 23.5 percent in the most recent survey. Over the same span, the portion of the panel that felt that the Fed has been too easy has declined to an almost invisible 2.4 percent. Continuing the trend of recent surveys, somewhat less than 60 percent of the respondents felt that the level of the federal funds rate was the best indicator of the current direction of monetary policy, while about 30 percent felt that recent money growth rates were the best indicator. These percentages have changed very little over the past year.

About 63 percent of the panel believed that monetary policy will be chiefly guided in the next 6 months by the rate of inflation (and inflation expectations). Another 26 percent thought that the pace of economic growth would be the primary determinant of policy. Despite the sharp rise in the value of the dollar through the survey period, only 8 percent of the panel thought that the Fed would be led primarily by exchange rates in the setting of monetary policy.

In contrast to policy surveys over the past year, a majority of the panel felt that the Fed would either keep monetary policy relatively unchanged or would ease by enough to cause the federal funds rate to drop. The largest group of respondents thought that the Fed would keep policy unchanged, nearly 40 percent, while the next largest group, about one-third, thought that the Fed would ease a bit. The degree of easing expected by this group was small, however, with only about 9 percent of the panel expecting a significant enough policy change to cause the discount rate to be cut. Respondents in previous surveys felt strongly that the Fed would be moving to tighten monetary policy, in line with expectations of higher inflation in the winter and spring. The most recent NABE Macroeconomic Survey, however, indicated that most business economists expect slower economic growth and lower inflation over the second half of this year. The policy survey result that monetary policy is unlikely to be tightened over the next 6 months is consistent with this expectation of slower growth and inflation.

The FSLIC Bailout Bill

One of the major differences between many in Congress and the Bush Administration on the FSLIC bailout bill is whether the bonds to finance the payout should come directly from the Treasury Department, or whether they should come from an off-budget agency such as the proposed Refcorp. The respondents in the NABE policy survey felt strongly that the bonds should be issued directly by Treasury, with nearly 64 percent favoring direct financing. Only about 21 percent thought that Refcorp financing would be appropriate. Another 15 percent felt that the funding mechanism did not matter.

The House bill proposes that direct Treasury financing not count against the Gramm-Rudman-Hollings deficit targets. The NABE policy panel, however, felt that the cost of such financing should count against the deficit targets, with 57 percent favoring this accounting. About 30 percent agreed with the House that the cost of the Treasury financing should not count against the Gramm-Rudman-Hollings targets, while another 13 percent felt that it did not matter.

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The panel agreed with many other portions of the House and Senate bills. An overwhelming 96 percent of the respondents felt that risk-based capital guidelines should be imposed on thrifts as part of the FSLIC bailout proposal. Of those that agreed with this proposition, more than 81 percent thought that the guidelines should be the same as those that commercial banks are subject to. Only 13 percent thought that thrifts should be subject to more stringent risk-based capital guidelines than banks, and a mere 5 percent thought that thrifts should be subject to less stringent guidelines.

Nearly 73 percent of the panel felt that thrifts should pay for some portion of the bailout plan through higher deposit insurance rates. More than 25 percent, however, felt that it would not be appropriate for thrifts to be forced to pay higher deposit insurance rates. About two-thirds of the panel thought that the regulatory and credit functions of the Federal Home Loan Bank Board should be divided, as is currently the case for commercial banks with the FDIC and the Comptroller of the Currency. Nearly 24 percent thought that such a division should not take place. There was only a small majority of the panelists, however, who thought that commercial banks should be allowed to take advances from regional Federal Home Loan Banks as long as they qualified under the "qualified thrift lender" rules.

The NABE policy panel felt strongly that portions of the bill that do not have direct applicability to the bailout should be excluded. In particular, nearly two-thirds of the respondents thought that the measure authorizing the regional Federal Home Loan banks to subsidize interest rates for member institutions to dedicate to low- and moderate-income housing should not be part of the bailout bill. About 21 percent of the panel thought that it was appropriate to include such a provision. Similarly, nearly 66 percent of the panel thought that a measure that would guarantee local housing agencies the right of uncontested bids for certain low cost residential properties seized from failed thrifts should not be a part of the bailout bill, while about 26 percent favored the inclusion of this provision.